

message from attorneys in charge

Our new *U.S.-India Update* focuses on U.S. legal developments of interest to Indian companies doing business in the United States and U.S. companies doing business in India. In each newsletter, we focus on specific topics across various practice areas that are particularly relevant to the U.S.-India business.

Pepper Hamilton's India practice is a multidisciplinary practice focused on inbound and outbound work with India in the areas of M&A, finance, private equity, securities, investment funds, tax, intellectual property, data privacy, outsourcing, compliance, FCPA, labor, employment, environmental, climate change and sustainability and other regulatory matters.

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Cross-Border Investments

India FDI: Are We Facing Another Case of Flip-flop?

The Congress Party's surprise victory in India's recent parliamentary elections has ushered in a strong surge in confidence in the Indian economy, resulting in an unprecedented 17.3 percent stock rally in the Indian capital markets that has caused those markets to rise 48 percent this year. Based on the Indian government's five-year track record under Prime Minister Manmohan Singh's leadership, the re-election of the Congress Party promises continued economic reforms in India and further opening of its economy to foreign investments.

At the forefront of these measures is the expected continued relaxation of the foreign direct investment (FDI) regime in India. Under the current regime, foreign direct investment in Indian companies is subject to sectoral limitations by industrial sectors, with foreign investments of up to 100 percent permitted in certain sectors (e.g., transportation infrastructure, electricity, pharmaceuticals) down to limits of up to 26 percent in others (e.g., insurance, defense, television news channels).

In February 2009, India's Ministry of Commerce and Industry amended certain guidelines for computing foreign direct investment in India. These amendments significantly increased the ability for foreign direct investment in India through step-down joint ventures. But the amendments have faced fierce criticism from, among others, the Reserve Bank of India and the Indian Finance Ministry's Department of Economic Affairs, which have raised objections to these Press Notes on the basis that they raise the possibility of "circumventing the definition of ownership and control by downstream investments" in sectors in which FDI is prohibited, government approval is required or sectoral caps are in place.

It is anticipated therefore that these Press Notes will be altered significantly in the near future. It is unclear, however, whether this will result in a return to the regime in place before these Press Notes were issued, or will simply result in ironing out some of the creases the Press Notes created. Yes, this could be another case of "flip-flop."

Specifics about the amendments is provided in our recent Client Alert, available at http://www.pepperlaw.com/publications_update.aspx?ArticleKey=1506.

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Market Conditions to Produce Significant Distressed M&A Opportunities in Second Half of 2009

The current economic downturn will offer greater discounts on distressed assets than previous downturns have offered, drawing both financial and strategic buyers to the market in the coming months, according to 92 percent of respondents to a new **Distressed M&A Outlook** survey conducted by mergermarket, Carl Marks Advisory Group LLP and Pepper Hamilton LLP.

In the second quarter of 2009, Carl Marks Advisory Group LLP and Pepper Hamilton LLP commissioned mergermarket to survey 75 investment bankers, private equity practitioners, hedge fund investors and lawyers regarding their outlook for distressed M&A activity in the upcoming year. Respondents provided invaluable insight into current market conditions, as well as a forecast for the year ahead.

“With a variety of factors contributing to an increased volume of distressed opportunities, both buyers and sellers are expected to eagerly pursue deals, as each side stands to gain unique benefits,” said Jim Rosener, managing partner of the New York office and head of the International Practice Group at Pepper Hamilton LLP.

Aside from attractive discounts, debt-related issues will likely be the most prominent drivers of distressed M&A activity in the upcoming year, according to respondents. An increase in covenant defaults is identified as a major catalyst to distressed deal flow, as is companies’ inability to meet debt obligations or refinance upcoming maturities.

Distressed investors are likely to find the greatest opportunity in the following two sectors:

- Real Estate, where 63 percent of respondents expect to see the highest volume of distressed deals in the year ahead.
- Financial Services, which 38 percent of respondents believe will experience the highest volume of distressed M&A this year.

Sixty-three percent of respondents expect most distressed deals to be handled outside of court; however, Chapter 11 reorganizations may be an exception as these are expected to be extremely common over the next 12 months.

The predominance of out-of-court deals is likely related to time constraints, as many respondents cite time as a major drawback to handling deals in court. Fifty-nine percent of respondents say the distressed M&A process can exceed four months when handled in court. Meanwhile, on cases handled outside of court, only 25 percent of respondents say the process can take this long. “If implementable, out-of-court solutions are generally less expensive and disruptive. However, it is not clear whether companies with complex capital structures will ultimately be able to obtain all of the consents necessary to use these solutions,” explains Duff Meyercord, partner at Carl Marks.

Time constraints also are expected to put pressure on management teams within distressed companies, which in turn may influence the dynamics of distressed transactions going forward. According to Jim Rosener, “Not only is the market characterized by people having to do something and forced to do it on a tight timetable, but there also is an increased opportunity as management loses focus and interest over these orphaned businesses.”

Additional findings:

Exit outlook: 65 percent of respondents plan to delay their exits from distressed investments in the upcoming year.

Valuations: 54 percent of respondents say asset-based valuations tend to be the primary determinant of price.

Alternative strategies: 79 percent of respondents expect debt buy-backs to increase in the year ahead.

If you would like a copy of this report, please visit <http://www.pepperlaw.com/news.aspx?AnnouncementKey=268>.

White Collar and Compliance

Guilty Verdict Highlights Importance of Due Diligence in International Transactions

The U.S. Department of Justice and the Securities and Exchange Commission have rapidly expanded enforcement of the Foreign Corrupt Practice Act (FCPA), which prohibits payments to foreign government officials to obtain or retain business, as well as entries in corporate books to conceal such payments. Investigations have hit a broad range of companies and industries, resulting in record-setting judgments.

This enforcement trend significantly affects Indian companies that have operations in the United States, raise capital in U.S. markets or seek joint ventures with U.S. companies as well as U.S. companies doing business in India. Understanding how liability arises, and what safeguards need to be in place, is critical to any Indian company conducting international business.

This area is particularly important as U.S. regulators continue to closely scrutinize business practices in India, and as officials and organizations in India push for corruption reforms. For example, the Indian Central Bureau of Investigation (CBI) recently cooperated with the Securities and Exchange Commission concerning bribes paid to Indian officials by a chemical company in order to get certain chemicals registered. The CBI followed up with a request to American authorities for evidence to further the CBI's own investigation of the bribe recipients in India. This cooperative sharing makes enforcement across international lines an easier task for all governments.

Private groups also are pushing reform in the Indian marketplace. For example, Transparency International has been working to have Indian companies sign an integrity pledge intended to eliminate corruption in the procurement process. As of April 2009, 37 countries have signed the pledge. Organizations ranging from the World Bank to the United Nations continue to focus on improving compliance standards to better enhance India's development opportunities.

Needless to say, complying with the FCPA in this environment presents challenges. Indian companies need to consider this carefully as the liability net is cast more broadly in this enforcement area. **Specifics on recent devel-**

Reminder - U.S. Identity Theft Regulation: Are Your Red Flags Rule Policies in Place?

On November 1, 2009, the U.S. Federal Trade Commission will begin enforcing its identity theft "Red Flags Rule." Under the rule, many financial institutions and creditors with "covered accounts" will be required to have policies to protect against and respond to identity theft. (The rule defines the term "creditors" as including businesses or organizations that have continuing credit or deferred payment relationships with any person or entity worldwide, and in this regard, the rule defines "creditors" differently than how industry generally understands the term.) For example U.S. entities that outsource work to India may be affected by the rule and could be required to have a written identity theft policy in place. In limited instances, non-U.S. companies also may be required to have such policies. "Covered account" means (1) an account primarily for personal, family or household purposes, that involves or is designed to permit multiple payments or transactions, or (2) "any other account" for which there is a "reasonably foreseeable risk to customers or the safety and soundness of the financial institution or creditor from identity theft" (a loosely defined, expansive concept).

Therefore, financial institution or creditors with covered accounts that do not have an identity theft policy, should learn whether the rule applies to them and if so, to put simple compliance policies in place to deal with regulatory and litigation risks. For further information, please contact Valérie Demont (1.212.808.2745), Janaki Rege Catanzarite (1.215.981.4532) or Matthew Silver (1.215.981.4117).

opments in U.S. law, and the implications for companies doing business in India are included in our recent *White Collar and Corporate Investigations Newsletter*, available at http://www.pepperlaw.com/publications_update.aspx?ArticleKey=1546.

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Sustainable Energy, CleanTech and Climate Changes

Climate Change Legislation: It's Time for Businesses to Take it Seriously

With strong backing from the Obama administration and congressional leadership, U.S. climate change legislation recently took a big leap toward passage on June 26, when the House of Representatives voted to adopt H.R. 2454, the American Clean Energy and Security Act of 2009. The bill now goes to the Senate, where the President and Senate leadership have vowed to amass the daunting 60 votes needed to enact this legislation before the end of the year.

The United States is under pressure to at least announce new climate change policies prior to or at the December 7-18, 2009 international climate change treaty meeting in Copenhagen. The U.S. failed to meet its goal set by the Kyoto Protocol of a 7 percent reduction between 1990 and 2012. In fact, U.S. emissions increased 17 percent between 1990 and 2007 (compared to 17.4 percent and 21.3 percent reductions in the United Kingdom and Germany during the same period), which has led to strong criticism from international environmental groups. With the dramatic changes brought by President Obama's electoral victory and substantial Democratic majorities in the House and Senate, there is every reason to believe a climate change regime is coming to the U.S. in the near future. Even if enacting legislation proves too difficult, the U.S. Environmental Protection Agency is poised to adopt regulations under the Clean Air Act that could well be more restrictive than the bills under consideration.

The U.S. climate change bill remains controversial and many additional concessions to economic reality will be necessary to secure its passage. But the legislation's striking success thus far has made it clear that companies must take very seriously the chances of far-reaching changes in virtually every aspect of the way they do business in the United States. The bill (a) uses a partially free and partially auctioned cap-and-trade system to reduce industrial emissions of carbon dioxide; (b) establishes more stringent energy efficiency requirements for products, industrial processes, and buildings; and (c) sets renewable energy standards for states, to encourage increased use of non-fossil fuels to generate electricity.

The cap-and-trade system will be complex and costly. Although the system allows any level of emissions as long as the company holds greenhouse gas (GHG) emission allowances or offsets that cover the amount of actual emissions, the cost of purchasing such allowances and offsets can be substantial, particularly if a company is not in the industrial sectors that qualify for a rebate of the cost of such emissions. Effects will spread beyond the sphere of environmental law, affecting activities involving energy, tax, securities, corporate merger and acquisition strategy, international trade, construction, real estate, intellectual property, and product marketing. For example, the U.S. Securities and Exchange Commission is looking into increased disclosure requirements regarding climate-change risks, and increases in natural disasters (allegedly due to climate change) are forcing insurance companies to change their financial models, from a focus on historic trends to anticipation of changing trends.

Increasingly, companies that operate in the United States are becoming alert to the need to undertake targeted climate change assessments. Of particular significance to Indian business interests, one provision in the existing bill allows the President to ban the import of goods from countries that do not have a climate-change regulatory scheme comparable to the U.S. system unless they hold international reserve GHG emission allowances to offset the carbon emitted during the manufacture of the goods. This provision is directed at developing nations and if India does not adopt a system similar to the U.S. climate change program, as appears likely, its goods could be subject to this "tariff." Savvy businesses may find opportunities in this coming wave of change, but in any event cannot afford to ignore it, even in their near-term planning.

More information about this issue is provided by our recent *Sustainability, CleanTech and Climate Change Alert*, available at http://www.pepperlaw.com/publications_update.aspx?ArticleKey=1549.

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Outsourcing and Intellectual Property

HITECH Act Aims to Create Nationwide Health Information Technology Infrastructure

The American Recovery and Reinvestment Act of 2009 (ARRA), effective on February 17, 2009, includes the Health Information Technology for Economic and Clinical Health (HITECH) Act, which focuses on developing a nationwide health information technology (HIT) infrastructure that supports electronic health records and health information exchanges. To accomplish this, the act provides for:

- creating standards, implementation specifications and certification criteria for network interoperability, and
- implementing the health network and electronic health records (EHRs) through grants, loan funds, incentive programs, and information sharing.

The HITECH Act is of great importance to Indian companies doing business in the U.S. health care sector as well as outsourcing providers servicing the U.S. health care industry.

The HITECH Act, recognizing that the successful adoption of HIT relies on privacy and security, includes provisions intended to enhance and strengthen the privacy and security of health information as it is received, created, processed, stored and transmitted over the nationwide HIT infrastructure. In this article, we focus on the act's privacy and security provisions, which include:

- clarification and expansion of the definition of a "business associate"
- increased business associate legal obligations
- enhancement of enforcement, funding for enforcement and increased penalties

- notification for breaches involving protected health information (PHI), and
- special provisions for vendors of personal health records and other non-HIPAA covered entities.

More information about this issue is provided in our recent *Client Alert*, available at http://www.pepperlaw.com/publications_update.aspx?ArticleKey=1416.

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Tax

Are There Sovereign Wealth Funds in India's Future?

Forced by the global credit crunch out of the shadow of international finance and into the bright glare of the public spotlight, investments by foreign sovereigns and, in particular, sovereign wealth funds (SWFs), have captured worldwide attention. This is no less so in India, where for the past several years, SWFs have been accepted as investors through the FII (Financial Institutional Investor) route. In the last five years approximately nine SWFs have invested in India this way. This article briefly explores the background of and policy concerns relating to SWFs, and describes the special United States tax regime applicable to

SWFs, in order to inform the current discussion in India concerning the emergence of SWF investment in that country.

The article is available at http://www.pepperlaw.com/publications_update.aspx?ArticleKey=1576.

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